

NEWS ANALYSIS

The new threat to Apple

It's just possible that Amazon could end Apple's domination of the music download market. Paul Nesbitt looks at its tactics and asks if the planned assault can work

It's an open secret that record companies are fed up with Apple's domination of the music download business. They want to free themselves from the 'one price fits all' model Apple insists on using. Most albums and pretty much every single that Apple sells costs the same. This is the opposite approach to that taken by the record industry, computer industry and most other businesses. Record labels would like to charge more for the latest hit singles and release bargain compilations of older and more obscure stuff.

Apple's perspective is that simplicity is one of the driving forces behind iTunes' success. It also believes that the music industry, with its history of shabby and greedy business practices, could quite easily kill the online music business by raising prices.

The music industry is looking for alternatives to Apple, but none of its competitors can match the unique combination of iPod and iTunes. Producing both hardware and software was not a winning formula for Apple in the PC market, but in the consumer electronics and entertainment markets, where people want easy-to-use and reliable products, it's the way to go.

"We believe Apple's key fundamental competitive advantage is its tightly integrated stack of home-grown hardware, software and service and the large installed base of 42 million iPods," said American Technology Research analyst Shaw Wu.

DO IT YOURSELF

The Xbox is another example of this trend. Microsoft tried to find hardware partners to produce a games console before concluding that the way forward was to build the whole thing, following the lead of Sony, Nintendo and Apple.

Now it looks as if the anaemic performance of music player manufacturers and online music services that use Microsoft's Windows Media software (which is pretty much all of them, with the exception of RealNetworks) is prompting a major rethink. After all, the fact that Microsoft decided to



launch the PlaysForSure accreditation shows that a lot of music players were not able to play what they were supposed to.

It's no surprise that the technology industry is buzzing with rumours that Microsoft is planning to produce its own music player, dubbed the xPod by analysts, to go head-to-head with Apple's iPod.

Wu warns that repeating its Xbox strategy is not without problems for Microsoft. "It would compete with its partners and customers. Moreover, we believe development of such a product would take a few quarters and it remains to be seen if it would succeed in the market."

So, if Microsoft can't pose a strong challenge, which company can? According to the *Wall Street Journal*, the answer lies with Amazon (www.amazon.com).

ALL MOD CONS

Amazon is good at selling over the internet and it sells a lot of CDs and DVDs. But with iTunes' success its business is suddenly looking vulnerable and, dare one say it, old-fashioned. This is a cardinal sin for new technology icons.

Physical products bring financial and time limitations. Apple can send music over broadband connections, while Amazon has to operate giant warehouses, with forklift truck operators moving palettes of CDs on to trucks. This is expensive, and it takes longer for customers to get their goods.

Amazon badly needs to add a successful music download business to its portfolio. Indeed, for a firm that some shareholders have criticised for the huge amounts it spends on R&D, it seems odd that Amazon is so late in entering the music-download market.

The company is determined to remedy this. "As we move forward with digital, we think Amazon is especially well positioned to capture a bigger part of that business," said Amazon's CFO Thomas Szkutak, although he declined to be more specific.

So what will Amazon bring to the music business? According to several music industry executives who attended talks with Amazon and were quoted anonymously by the *New York Times*, Amazon plans to offer a subscription service.

But hang on, that's not very exciting. RealNetworks, Napster, AOL and Yahoo! offer subscription services, and they have about two million customers between them. Meanwhile, Apple is about to sell its billionth download.

On the other hand, Amazon has a customer base of over 55 million regular users, compared with Napster and RealNetwork, which have customer bases of between 500,000 and 600,000. Amazon has the clout to make an impression.

According to insiders familiar with Amazon's plans, the firm has decided to bite the bullet and sell its own Amazon-branded music player to compete with Apple.

Amazon will design the player and have it built by a consumer electronics vendor. The idea is that it will work seamlessly with Amazon's proprietary software.

PERSONAL SERVICE

Amazon also plans to make the most of its customer database. It stores information on every item it has ever sold you, so its recommendations of music you might like could be preloaded on your Amazon music player. Amazon is also talking to record labels about selling music CDs at a discount to customers of its music subscription service. As Amazon already sells music CDs in large volumes, it has considerable bargaining power in this area.

Amazon is also looking at preloading its music players with free digital versions of music customers have already bought on CD, saving them the hassle of transferring their own music. The new service is expected to launch this summer in the US, and before the end of this year elsewhere.

It's interesting that the music business gives Amazon's late entry into the download market so much credence, especially as it looks like a copy of Apple's proprietary model rather than the Windows Media Audio model, where music players and online stores can all work together (if not particularly well).

Amazon will bring its expertise and online infrastructure, but it will need to find someone who can build an iPod killer. NPd analyst Ross Rubin notes that so far other attempts to do this have failed, including Samsung's Napster-branded music player. Samsung is the firm most people are tipping to make Amazon's music player.

Amazon's best chance of overcoming the iTunes/iPod stranglehold could be to borrow a strategy from mobile phone operators. According to the *Wall Street Journal*, the firm is looking to the mobile market for inspiration. Amazon will sell its music players at a discount if you sign up for its subscription service for a certain period. Or it may give them away for free. You can't beat free. **CS**